Supreme Court, U. S.
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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1978

No. 78-1062

THOMAS K. McMANUS and
MARGARET F. McMANUS, ET AL,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF
APPEALS FOR THE NINTH CIRCUIT

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ESTATE OF JOHN C. GUTLEBEN, Deceased,
UNITED CALIFORNIA BANK, Executor, and
VERA B. GUTLEBEN, Surviving Wife,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent,

ESTATE OF ELEANOR B. CHICK, Deceased,
ESTATE OF NELSON H. CHICK, Deceased,
NELSE CHICK SILER, Executrix, and
DOROTHY W. CHICK,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent,

PETITION FOR WRIT OF CERTIORARI
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Thomas K. McManus, Margaret P. McManus, Estate of John C. Gutleben, United California Bank, Vera B. Gutleben, Estates of Nelson H. and Eleanor B. Chick, Nelse Chick Siler and Dorothy W. Chick, petitioners herein, pray that a Writ of Certiorari issue to review the per curiam judgment of the United States Court of Appeals for the Ninth Circuit, entered in the above-entitled case on October 4, 1978.

CITATIONS TO OPINIONS BELOW

The opinion of the Tax Court of the United States is reported at 65 T.C. 197 (1975) and is reproduced in Appendix A hereto. The opinion of the Court of Appeals for the Ninth Circuit is currently not officially reported. It is unofficially reported in 78-2 U.S.T.C. ¶9748, and is reproduced in Appendix B hereto.

JURISDICTION

The judgment of the Court of Appeals was made and entered on October 4, 1978. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

QUESTION PRESENTED

Condemned land under the eminent domain power of the State of California cannot be sold except to the State of California. (1) After two years of fighting over the amount of the award, are the net proceeds granted to an unwilling seller, to be

e.g. land condemned under eminent domain power Calif.

taxed as capital gain or ordinary income? The decision below held ordinary income. The decision is ERRONEOUS. Taxpayers have no choice of to whom to sell their property. Once the State of California decides to exercise its power of eminent domain, the taxpayer is in its hands and the hands of its Courts.

The taking of property has been a right of governments from ancient history. The right of a government to take any citizen's property was embodied in the Fifth Amendment to the United States Constitution (ratified 1791), "...nor shall private property be taken for public use, without just compensation."

(2) Is a governmental taking under the Bill of Rights a sale in the "ordinary course of business" as defined by the Internal Revenue Code? Remember the sale to the State of California was NOT voluntary.

California, a sovereign state having Courts of original jurisdiction also has a similar provision. We, California, can take your property any time we want to; the California Constitution provides (Article I, Sec. 19):

> "Private property may be taken or damaged for public use only when just compensation... has first been paid to...the owner." (Emphasis added)

If the above be a sale in the "ordinary course" of the taxpayers' trade or business, there must be a mistake in either the English language or in the Internal Revenue Code. If a condemnation transac-

tion must be sanctioned by the Constitution of the United States and the Constitution of the State of California, it cannot be "ordinary." Why else were the Constitutional provisions necessary?

STATEMENT OF THE CASE

In 1961, petitioners McManus, Chick and Gutleben purchased a thirty-six and one-half (36-1/2) acre tract of undeveloped land on Hegenberger Road in Oakland, California for about $926,000.00 (Tract 2347). Title was taken in the individual names of McManus, Chick and Gutleben (Ex. 11-K). Petitioners purchased Tract 2347 to develop it for leasing to tenants with the hope that it would appreciate in value and to provide work for two construction companies of which the taxpayers were equal controlling shareholders. They believed that future lessees would hire petitioners' construction companies to erect improvements needed thereon.

But taxpayers were frustrated by the 1967 condemnation action taken by the State of California.

As early as 1965 the taxpayers received a letter from the State of California Division of Highways indicating the location of a proposed road to be constructed directly through the taxpayers' property. After several months elapsed without any further action by the state, the taxpayers wrote the State voicing the following concern:

> The postponement of the acquisition and the actual

> construction while the property remains earmarked for condemnation is seriously and adversely affecting our use of the property as well as its present saleability.

Despite the hardship imposed by the prolonged wait, the State did not ultimately take the property by way of eminent domain until three years later in 1968. Not only were the taxpayers' original development plans frustrated, but during the entire period the property was held for sale to one customer only, the State of California. Furthermore, even after the condemned portion was taken, the resultant fragmentation of the taxpayers' land left them with several inaccessible remnant portions which in one case necessitated an exchange of a new parcel for one previously sold.

The taxpayers filed individual petitions in the Tax Court in response to statutory Notices of Deficiency issued by the Commissioner of Internal Revenue for deficiencies assessed in federal income taxes for calendar years 1968, 1969, 1970 and 1971. The cases were consolidated for trial and briefing.

The Tax Court held that the property was acquired and held primarily for sale to customers in the ordinary course of petitioners' trade or business and that the net proceeds of the condemnation sale were taxable as ordinary income. The Tax Court ignored the three year period caused by the filing of the condemnation action by the State of California. The involuntary taking of property is hardly a "sale" to customers in the "ordinary course" of the

taxpayers' trade or business. I.R.C. §1221(1) is explicit on "ordinary course."

In condemnation, you sell whether you want to or not. That's not the "ordinary course" of anyone's trade or business. Condemnation of your land is a "no choice situation." A taxpayer is lucky if he gets fair market value after a difficult struggle, attorney fees and Court costs. In this particular case, it took three years before the State of California raised the "award" to a reasonable amount. In the meantime the property was tied up.

If that was a transaction in the "ordinary course" of the taxpayers' trade or business, this Court will define what is an "extraordinary" transaction in the course of business.

REASONS FOR GRANTING THE WRIT

The decision below on the question of whether or not the proceeds received as a result of condemnation of the taxpayers' property by the State of California were to be afforded capital gains treatment is in direct conflict with the Court of Appeals for the Fifth Circuit in Ridgewood Land Co., Inc. v. Commissioner, 477 F.2d 135 (C.A. 5, 1973), aff'g per curiam P-H Memo T.C. par. 72,016 (1972) and with the Court of Appeals for the Tenth Circuit in Commissioner v. TRI-S Corp., 400 F.2d 862 (C.A. 10, 1968).

I. WHERE THE TAXPAYER ACQUIRES REAL PROPERTY AND SUBSEQUENT CONDEMNATION MAKES THE ORIGINAL ACQUISITION PURPOSE IMPOSSIBLE TO ACHIEVE, THE DISPOSITION TO THE CONDEMNOR IS TO BE TREATED AS THE SALE OR EXCHANGE OF A CAPITAL ASSET.

The Tax Court held that the condemnation by the State of California did not change the taxpayers' purpose in holding the property to one for investment -- the taking by the State was a sale made in the ordinary course of a business. The Ninth Circuit affirmed, relying on Juleo, Inc. v. Commissioner, 483 F.2d 47 (3rd Cir., 1973).

However, both the Fifth Circuit in Ridgewood Land Co., v. Commissioner, 477 F. 2d 135 (5th Cir., 1973) and the Tenth Circuit in Commissioner v. TRI-S Corp., 400 F.2d 862 (10th Cir., 1968) hold to the contrary. If the taxpayer or owner is forced to abandon his original purpose in acquiring the property, the finding is tantamount to a finding that the taxpayer has changed his intentions regarding his purpose for holding the property. Therefore, when condemnation occurs, by actual notice here; the taxpayer-owner cannot hold property for sale to customers, regardless of his original intent.

Since the taxpayers' original purpose in acquiring the property was substantially, if not "primarily", to lease the property, or at worst, to sell the property to a tenant or buyer who would employ the taxpayers' construction companies to erect improvements thereon, the condemnation by the State clearly made

this purpose impossible: the State was under no obligation to employ the taxpayers' construction companies and, but for the condemnation, the taxpayers were free to choose a tenant (or purchaser) who would agree to purchase their construction services.

The inescapable conclusion is that as soon as the taxpayers became aware of the State's plan to acquire the property, the threat of condemnation was real, the taxpayers' purpose for holding the property was frustrated and the involuntary disposition to the State was a sale of property no longer held for sale to customers in the ordinary course of business.

CONCLUSION

For the foregoing reasons, this petition for a Writ of Certiorari should be granted.

Dated: December 27, 1978

Respectfully submitted,

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APPENDIX A

65 T.C. 197

UNITED STATES TAX COURT

THOMAS K. McMANUS and MARGARET F. McMANUS, ET AL.,[1/] Petitioners, v. COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket Nos. 2879-73, 2880-73
2881-73, 8593-73
8594-73, 8595-73

Filed October 30, 1975

Messrs. McManus, Gutleben and Chick acquired a tract of land in the industrial section of Oakland, California. The property was subdivided and improved and portions of it were sold. Two of these sales were attributable to condemnation activity. Held: The entity created by the petitioners constitutes a

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1/ Cases of the following petitions are consolidated herewith: Estate of John C. Gutleben, Deceased, United California Bank, Executor, and Vera B. Gutleben, Surviving Wife, Docket Nos. 2880-73 and 8594-73; Estate of Eleanor B. Chick, Deceased, Nelson H. Chick, Surviving Spouse, Docket No. 2881-73; Thomas K. McManus and Margaret F. McManus, Docket No.8593-73; Nelson H. Chick and Dorothy W. Chick, Docket No. 8595-73.

partnership. Held further: The partnership acquired and held the property primarily for sale to customers in the ordinary course of its trade or business. Held further: The condemnation activity does not change the purpose for which those portions of the property involved were held by the partnership. Juleo, Inc. v. Commissioner, 483 F.2d 47 (3d Cir. 1973); Ridgewood Land Co. v. Commissioner, 477 F.2d 135 (5th Cir. 1973); and Commissioner v. TRI-S Corp., 400 F.2d 862 (10th Cir. 1968) distinguished. Held further: The individual election pursuant to section 1033 by petitioner McManus to defer the gain realized on a condemnation sales is ineffective since that election must be made by the partnership.

During the course of respondent's audit, the petitioners signed a form purporting to extend the statute of limitations with respect to their timely filed 1968 individual tax returns until 90 days after either party notifies the other that they wish to terminate the agreement. Held: This agreement was reasonably used in this instance.

Paul E. Anderson and C. Henry Veit, for the petitioners.

Nicholas G. Stucky and Lamont R. Olson, for the respondent.

STERRETT, Judge: The respondent determined deficiencies in petitioners' federal income taxes as follows:

Docket Number	Petitioner	Year	Deficiency
2879-73	Thomas K. McManus and Margaret F. McManus	1968	$43,235
		1969	1,120
8593-73	" " "	1970	22,129
		1971	4,074
2880-73	Estate of John C. Gutleben Deceased, United California Bank, Executor, and Vera B. Gutleben, Surviving Wife	1968	21,897
		1969	1,577
8594-73	" " "	1970	22,510
2881-73	Estate of Eleanor B. Chick, Deceased, Nelson H. Chick, Executor, and Nelson H. Chick, Surviving Spouse	1968	25,538
		1969	1,667
8595-73	Nelson H. Chick and Dorothy W. Chick	1970	22,622

Upon petitioners' oral motion, to which respondent had no objection, these cases were consolidated for trial, briefs and opinion. The issues in controversy common to these cases are whether Thomas K. McManus, John C. Gutleben, and Nelson H. Chick were conducting their activities with respect to a tract of land as individuals or as a partnership, whether the gain realized from the sale of portions of this land, including a condemnation sale, held by the petitioners either as individuals or in a partnership should be characterized as ordinary income or capital gain, and whether the consent agreements (Treasury Form 872-A) executed by the petitioners purporting to extend the statute of limitations for the taxable year 1968 are

valid. In connection with the partnership issue, we must determine whether the election made under section 1033[2/] by petitioners Thomas K. McManus and Margaret F. McManus is sufficient to defer the gain that was realized in 1968 on a condemnation sale of a portion of the land or whether this election could only be properly made by the partnership if one existed.

FINDINGS OF FACT

Some of the facts have been stipulated and are so found. The stipulation of facts, together with the exhibits attached thereto, are incorporated herein by this reference.

Petitioners Thomas K. McManus (hereinafter petitioner) and Margaret F. McManus are husband and wife who resided in Berkeley, California at the time of the filing of their petitions herein. They filed timely joint federal individual income tax returns for 1968, 1969, 1970, and 1971 with the internal revenue service center at Ogden, Utah.

Attached to the 1968 tax return, as introduced into evidence, is a Special Consent Fixing Period of Limitation.

Upon Assessment of Income Tax (hereinafter Form 872-A) which was cosigned by them on December 30, 1971. Form 872-A provides in relevant part:

> That the amount(s) of any Federal income tax due under any return(s)

2/ All statutory references are to the Internal Revenue Code of 1954, as amended.

made by or on behalf of the above-named taxpayer(s) for the tax year(s) ended

December 31, 1968

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under existing or prior revenue acts may be assessed at any time on or before the 90th day after (1) mailing by the Internal Revenue Service of written notification to the taxpayer(s) of termination of Appellate Division consideration, or (2) receipt by the Regional Appellate Division branch office considering the case of written notification from the taxpayer(s) of election to terminate this agreement, except that if in either event a statutory notice of deficiency in tax for any such year(s) is sent to the taxpayer(s), the running of the time for making any assessment shall be suspended for the period during which the making of an assessment is prohibited and for 60 days thereafter. If such statutory notice is sent to the taxpayer(s) and neither of the conditions enumerated (1) and (2) in the preceding sentence have occurred, the time for making such assessment will expire 60 days after the period during which the making of an assessment is prohibited. However, this agreement will not reduce the period of time otherwise provided by law for making such assessment.

The statutory notice of deficiency is Docket No. 2879-73 is dated March 23, 1973.

John C. Gutleben (hereinafter Gutleben) and Vera B. Gutleben were husband and wife

and at the time of the filing of the petitions herein Vera B. Gutleben resided in Castro Valley, California. Gutleben died in September 1972 and the petitions herein have been filed by his estate and his surviving spouse. Gutleben and his spouse filed timely joint federal individual income tax returns for 1968, 1969 and 1970. Attached to the 1968 tax return, again as introduced into evidence, is a Form 872-A, cosigned by them on December 31, 1971. This Form 872-A is similar to the one noted above. The statutory notice of deficiency in Docket No. 2880-73 is dated March 23, 1973.

During 1968 and 1969 Nelson A. Chick (hereinafter Chick) and Eleanor B. Chick were husband and wife. At the time the petition herein for years 1968 and 1969 was filed, Eleanor B. Chick was deceased and Chick resided in Berkeley, California. During 1970 Chick and Dorothy W. Chick were husband and wife who resided in Berkeley, California at the time the petition herein for 1970 was filed. Chick and his spouse filed joint federal income tax returns for 1968, 1969, and 1970. Attached to the 1968 tax return, as submitted into evidence, is Form 872-A, signed on February 23, 1972, by Chick in his individual capacity and as executor of the estate of Eleanor B. Chick. This Form 872-A is similar to the ones noted above. The statutory notice of deficiency in Docket No. 2881-73 is dated March 23, 1973. Chick died in January, 1975.

Petitioner, Gutleben, and Chick (hereinafter the taxpayers) were all experienced in the construction engineering business. Petitioner met Chick in California in approximately 1936. They organized the Underground Construction Company which specialized

in underground utility work. This Company was incorporated in 1952.

Petitioner and Chick met Gutleben in approximately 1937. He became an employee of their company serving as a superintendent on one of their projects and later he acquired an interest in the company. These three men along with a fourth man then organized MGC Company (hereinafter MGC) which specialized in the construction of industrial and commercial buildings. This company was incorporated in 1955.

In September, 1961 the taxpayers purchased a tract of land in Alameda County, California consisting of approximately 36-1/2 acres for $926,000 (hereinafte Tract 2347 or the property). This property is situated in the northeast interchange of Hegenberger Road and Nimitz Freeway. It is near the Oakland Coliseum Arena and Exhibit Hall complex, the Bay Area Rapid Transit's Coliseum station, and the Oakland International Airport. This property represented prime industrial real estate. Title to the property was placed in all of their names as individuals.

Shortly after the acquisition was made the taxpayers applied to the city planning commission for approval to subdivide the property. The appropriate drawings and plans were submitted and their plans were subsequently approved. A subdivision plat map for the property was filed and recorded in May, 1962. This map reflects provision for 14 separate plots and a street intersecting the property.3/

3/ One of these plots was set aside for

Between March and September, 1962, approximately $240,000 was expended by the taxpayers in improving the property. These improvements included expenditures for road construction and the installation of sewerage, water, gas, and electrical facilities. The construction activities were completed by September, 1962.

Also during this time period the taxpayers engaged the services of the Stanford Research Institute, Menlo Park, California (hereinafter SRI) to make a preliminary study of the market for office space for a modern office building at the property's location. SRI prepared a report based on numerous interviews and extensive research.

SRI found that the rental market in Alameda County was generally depressed, but it did find a selective demand for a rental building that offered certain advantages and it believed that the building contemplated by the taxpayers could attract a portion of that demand. However, it felt that a structure of only 10,000 square feet of net rentable space was justified due to the generally depressed market and the pioneering aspects of a building at the proposed location, and that it would have to be built on a speculative basis.

During the years 1961 through 1970, financial transactions pertaining to the

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3/ (Continued)
the construction of a Holiday Inn. Negotiations with respect to this transaction began before the property was actually acquired so the necessary land was set aside and was not a part of the subdivision scheme.

property were recorded in books and records consisting of a double entry system of accounting. The property itself was reflected as an asset of McManus, Gutleben, and Chick. Several pages from a ledger account labeled "Capital" reflect various activity in this account.

Among the entries in the account are several labeled "Drawing 3 partners".[4/] Such drawings were always made in equal amounts to the individual taxpayers and it was their intention to divide equally the profits from their activities. In 1967 the taxpayers opened a checking account at the United California Bank, San Leandro, Calif. The signature card, which is still currently on file, indicates that these men were co-partners and the card is signed by them in their capacities as partners.

Partnership income tax returns in the name of McManus, Gutleben, and Chick were filed each year during at least the years 1961 through 1970. All of these returns were prepared and signed by Wesley T. Benson, a Certified Public Accountant (hereinafter Benson), and all of the returns were signed by petitioner. After 1970 the filing of partnership returns was discontinued on the advice of legal counsel. The activity with respect to the property was reported directly on petitioner's 1971 individual tax return.

During the course of his audit there was correspondence between the petitioners

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4/ The actual language of the individual entries varies, but the term "partner" is generally used. However, in June, 1974 the entry is labeled "owners drawings".

and respondent. In one such letter prepared by legal counsel and signed by petitioner and Margaret F. McManus, on June 2, 1969 as a protest to proposed adjustments in their 1967 tax return, they state that the petitioner was "a member of two partnerships, known respectively as McManus, Gutleben & Chick and Real Estate Joint Holdings. During the year 1967, said partnerships sold three parcels of real property *** ". Further on they refer to two of the parcels as being owned by McManus, Gutleben, and Chick. A second letter dated April 7, 1971, was prepared by Paul E. Anderson, legal counsel in this case and signed by the McManus', to protest proposed changes to their 1968 and 1969 tax returns. The letter protests the respondent's attempt to change their "allocable share of capital gain from the land holding partnership of McManus, Gutleben and Chick to ordinary income". In the remaining parts of the letter the entity holding Tract 2347 is referred to as a partnership and its members as partners.

The partnership returns indicate that the taxpayers started their business activity on January 1, 1954. These men along with their wives acquired a tract of land situated southwest of the intersection of Hegenberger Road and the Nimitz Freeway. Upon application to the city planning commission this tract was subdivided into several plots. Two streets and utilities were also installed. The appropriate documents were sent to the commission with a covering letter signed by petitioner as a partner on behalf of the taxpayers. These parcels were all sold with the last sale occurring in 1960.

The partnership income tax return for 1962 reported four sales from Tract 2347.

Gain was realized on all of these transactions and it was reported as ordinary income. One of these transactions was a sale by the taxpayers to a partnership known as Three Companies, which in turn sold the parcel to a third party who constructed the Holiday Inn. This partnership consisted of three corporations controlled by petitioner, Gutleben, and Chick, or their families, in their individual capacities. Other sales from Tract 2347 were made with one occurring in 1964 and two occurring in 1967. The gains realized from these transactions were reported as long-term capital gain.5/

In 1965 a parcel in Tract 2347 was transferred by the taxpayers to a partnership known as Real Estate Joint Holdings (hereinafter REJH). The taxpayers were equal partners. Subsequently, a building was erected on the parcel by MGC. Upon completion the building was leased by the Blue Chip Stamp Company. In 1967 REJH sold this building to a third party and realized a profit on the sale. This building was the only one constructed for rental purposes by the taxpayers, although MGC did construct buildings for others on Tract 2347.

During this time the taxpayers attempted to lease portions of Tract 2347 to several groups. There were negotiations with representatives of banks, a food store, a manufacturing company, the government with respect to a post office, and several other

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5/ The gain realized from the sales that occurred in 1967 was reported as long-term capital gain realized from the sale or exchange of property under sec. 1231.

parties. Portions of Tract 2347 were leased for an amusement ride, parking space, an outdoor sign, a model home display, and pipe storage. The total rental income from these sources during this period was nominal.

During this period it was generally known among real estate brokers that Tract 2347 was available for industrial or commercial development and was available for sale or lease. Real estate commissions were paid by the taxpayers on eight of the sales from Tract 2347 to various real estate agents or firms. On one occasion Gutleben gave one real estate firm the exclusive right for a period of approximately 45 days to sell a portion of the property. The taxpayers did not place a "For Sale" sign on the property.

The property was the subjecct of advertisements in magazines that listed such property. One such publication was prepared by the California State Chamber of Commerce and the following notice appeared in five of its publications between 1964 and 1970:

> Empire City Industrial Park--Oakland 1962; 36 acres; Light Industrial & Commercial. McManus, Chick & Gutleben, 2600 Williams Street, San Leandro

The purpose of this publication is to generate industrial growth in the state and it is sent to those firms involved in industrial development. Its circulation is approximately 8,000. The listing is free and the information is gathered from various sources throughout the state. Once a property is listed the publication is sent to the property owners and a card is sent prior to the issuance of the next publication so

that any new developments can be included. At the owner's request the notice is removed.

Other notices of this type also appeared in the April, 1969 Western Real Estate News, a publication mainly for realtors, contractors, architects, and engineers and the California Site Selection Handbook. The latter publication was prepared by the editors of Industrial Development Magazine, Conway Research, Inc., Atlanta, Georgia. Approximately 15,000 issues were circulated primarily to subscribers of the magazine and to persons in the real estate industry. The listings were compiled from questionnaires completed by the owners of the properties without cost to them. There is no evidence that any of the taxpayers ever completed such a questionnaire nor authorized in any other manner the description that appears in the handbook.

The partnership income tax returns for 1968, 1969, and 1970 reported the following sales from Tract 2347:

Year	Buyer	Gain	Total
1968	State of California	$200,989	
1968	Radio Corp. of America	42,482	$243,471
1969	Radio Corp. of America	$ 16,230	$ 16,230
1970	International Brotherhood of Boilermakers, et al	$ 71,111	
1970	Shell Oil Company[6/]	67,421	
1970	State of California	221,636	$360,168[7/]

6/ This transaction was an exchange of properties between the taxpayers and Shell Oil Co. The taxpayers received land, which they had

All of these gains were reported as long-term capital gains on the respective partnership returns and the total long-term capital gains for each year, along with the ordinary income or loss, was divided evenly between the taxpayers and reported by them as income received from a partnership on the respective individual tax returns.

The sale in 1968 to the State of California was pursuant to a condemnation action. In connection with this transaction, Gutleben wrote a letter on behalf of McManus, Gutleben, and Chick in March 1966, to the State of California in which he stated:

> The postponement of this acquisition and the actual construction while the property meanwhile remains earmarked for condemnation is seriously and adversely effecting our use of the property as well as its present saleability.

In November, 1968 petitioner purchased property in Fremont, California which he believed constituted replacement property under section 1033. Petitioner did not report his ratable share of the gain from the condemnation sale on his 1968 individual tax return. MGC constructed a building on this property

6/ (Continued)

previously sold to the Shell Oil Company plus $68,000 which after the deduction of expenses of $579 resulted in the above gain.

7/ The partnership return for this year reported $361,168 of long-term capital gain. The error, apparently one of addition, is not in issue.

which is currently being used by a third party. Petitioner did not notify the respondent or the Secretary of the Treasury or his delegate that he had purchased replacement property until after April 1, 1970.

In 1973 two additional sales of Tract 2347 were made by the taxpayers. One was a large sale to Continental Development Company that resulted in a gain of $960,749. These sales represented the final portions of Tract 2347 originally owned by the taxpayers, although they did own a portion through REJH. By 1973 Gutleben had passed away and Chick was in ill health and was contributing very little to the management of these affairs.

The respondent in his deficiency notices to the petitioners for the years in issue determined that the long-term capital gains as reported on the partnership returns and subsequently carried forward to the individual tax returns should properly be characterized as ordinary income. He explained his determination as follows:

> It is determined that such real property was held for sale to customers in the ordinary course of your trade or business. Accordingly, such profits are includable in ordinary income.

Respondent made the necessary changes in petitioners' tax returns to reflect this determination.

Respondent, with respect to petitioner's 1968 tax return, determined that the gain realized on the condemnation sale to the State of California as reported on the 1968 partnership tax return was taxable to the

petitioner in 1968 and that it represented ordinary income. He explained this determination as follows:

> ***It is further held that the sale to the State of California does not qualify for non-recognition of gain pursuant to section 1033 because the partnership made no election under section 1033(a)(3)(A) nor was replacement of the property made by the partnership in accordance with section 703(b).
>
> It is further held that the alleged replacement real property acquired individually by you does not qualify as replacement property within the meaning of section 1033 because it was not of a like kind or similar or related in service or use to the property acquired by the State of California.

Petitioners in an amendment to their petitions in Docket Nos. 2879-73, 2880-73, and 2881-73 allege that the notice of deficiency issued by the respondent is erroneous because it is barred by the statute of limitations. In his answer respondent denies this allegation.

OPINION

The case at bar requires us to consider procedural and substantive matters involving the years in issue before this Court. In order to dispose orderly of these issues we believe that the procedural issue should be discussed and determined at the outset.

Petitioners in amendments to their petitions filed in Docket Nos. 2879-73, 2880-73, and 2881-73 assert that the deficiency notices issued by the respondent with respect to 1968 are erroneous because that year is barred by the statute of limitations. The facts with respect to this issue are mainly uncontested.

The petitioners all timely filed their respective individual tax returns for 1968 and hence the standard 3 year statute of limitation would have expired on April 15, 1972 absent the prior execution of valid extensions. Section 6501(a),(b) and (c). Attached to these tax returns as introduced into evidence, are Forms 872-A, the relevant portion of which has been set out in our findings of fact. This form purports to extend the statute of limitations until 90 days after either party appropriately notifies the other that they wish to terminate the agreement. These agreements were executed in Docket Nos. 2879-73, 2880-73, and 2881-73 on December 30, 1971, December 31, 1971, and February 23, 1972, respectively. The respondent's notices of deficiency for these docket numbers are dated March 23, 1973.

Petitioners attack the validity of the open-ended nature of these agreements arguing that the use of the term "period" in section 6501(c)(4)[8/] requires that the term

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8/ SEC. 6501(c)(4). Extension by agreement. -- Where, before the expiration of the time prescribed in this section for the assessment, of any tax imposed by this title, except the estate tax provided in Chapter 11,

for which the statute of limitations is extended must be fixed and may not be indefinite. Petitioners do not cite any authority for this proposition, but rely mainly on dictionary definitions of the word "period".

Upon examination of the statute we see no requirement that the statute of limitations can only be extended for a definite period of time. The statute, in fact, does allow for additional extensions of the statute of limitations beyond the period of the agreement.[9/] As noted previously Form 872-A does permit the taxpayer to terminate the

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8/ (Continued)

both the Secretary or his delegate and the taxpayer have consented in writing to its assessment after such time, the tax may be assessed at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon.

9/ In Rev. Proc. 71-11, 1971-1 C.B. 679 the respondent explained that the agreement as used in this case was adopted.

*** to relieve taxpayers and the Service from the irritations and difficulties of obtaining renewal consents, to relieve the Service, in part, of the problems of maintaining controls to ensure that the period of limitation does not expire during consideration of a case, and to provide a means of restricting the period of limitation to the minimum time required for Appellate Division consideration, *** .

agreement upon proper notification to the respondent.

An agreement of the type in issue may very well not toll the statute of limitations indefinitely. This Court has held in several early cases that "an unlimited waiver extends the statutory period for a reasonable time, or until termination by either party upon reasonable notice". Ethel D. Co., 27 B.T.A. 25, 27-28 (1932), affd. 70 F.2d 761 (D.C. Cir., 1934). See also William S. Doig, Inc., 13 B.T.A. 256, 260 (1928); F. L. Bateman, 34 B.T.A. 351, 358 (1936). In Greylock Mills v. Commissioner, 31 F.2d 655, 658 (2d Cir. 1929), affirming 9 B.T.A. 1281 (1928), cert. denied 280 U.S. 566 (1929) the court said:

> But there is also another ground equally fatal to appellant's contention. If waivers which are in terms unlimited are to be limited at all, we think they should expire only after the taxpayer gives notice to the Commissioner that he will regard the waiver as at an end after a reasonable time, say three or four months, from the date of such notice. In such a rule there is no harshness to either party; on the contrary, it seems to us the most reasonable one. ***

In this case the agreements were executed between December, 1971 and February, 1972, the normal statute of limitations expired in April, 1972, and the deficiency notices which involved items common to 1968 and 1969 were issued in March, 1973. There is no indication in the record that the petitioners ever notified the respondent of

a desire to terminate the agreement or complained of unreasonable delay. We believe that the agreements have clearly been reasonably used in the case at issue and should be upheld. Consequently we believe that we should move on to a consideration of the substantive issues as they affect 1968 and the other years in issue.

The remaining issues common to the petitioners relate to their activities with respect to Tract 2347. We must decide whether the taxpayers conducted these activities as individuals or as a partnership and whether the gain realized from the sale of portions of Tract 2347, including a condemnation sale, by the taxpayers either as individuals or as a partnership should be characterized as ordinary income or capital gain.

As provided by section 761(a) "the term 'partnership' includes a syndicate, group, pool, joint venture or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on". The regulations expand and explain this definition and include other groups not commonly called partnerships.10/

10/ Sec. 1.761-1(a), Income Tax Regs.:

*** A joint undertaking merely to share expenses is not a partnership. For example, if two or more persons jointly construct a ditch merely to drain surface water from their properties, they are not partners. Mere coownership of property which is maintained, kept in repair, and rented or leased does not constitute a partnership. For example, if an individual owner, or tenants in common, of farm property lease it to a farmer for a cash

As noted by the regulations mere co-ownership of property does not cause the creation of a partnership. However, co-owners may be partners if the determination is made that they intended actively to carry on the business or venture as a partnership. Mihran Demirjian, 54 T.C. 1691 (1970), affd. 457 F.2d 1 (3d Circ. 1972), George Rothenberg, 48 T.C. 369 (1967). The burden of proof is upon the petitioners. George Rothenberg, supra. In the present case we believe the evidence shows that the taxpayers did intend to carry on actively their business affairs as a partnership, that they so held themselves out, and that the latter part of section 1.761-1(a) applies to the situation at hand.

The entity known as McManus, Gutleben, and Chick was organized by the taxpayers in 1954. After purchasing a tract of land, plans were submitted to the planning commission to subdivide certain property on two separate occasions. One set of plans was accompanied by a cover letter signed by petitioner as partner on behalf of the taxpayers. Improvements were made to the tract and the individual plots were sold by 1960.

10/ (Continued)

rental or a share of the crops, they do not necessarily create a partnership thereby. Tenants in common, however, may be partners if they actively carry on a trade, business, financial operation, or venture and divided the profits thereof. For example, a partnership exists if coowners of an apartment building lease space and in addition provide services to the occupants either directly or through an agent. ***

After completing their activity with respect to this tract, the taxpayers then acquired Tract 2347. Subdivision plans were again submitted on their behalf and improvements were made to the property. The taxpayers were involved in numerous business negotiations with respect to the property. Some of these negotiations resulted in rental and sale agreements. These negotiations were handled primarily by either petitioner or Gutleben, each with at least the apparent authority to make a commitment for the others.

From 1961 through 1970 partnership tax returns were filed in the name of McManus, Gutleben, and Chick. These returns reflect the various sources of income and expenses and the equal division of the net gain or loss. The accountant who prepared these returns testified that it was always the taxpayers' intention to share equally in this venture. Books and records were also kept in the partnership name and the capital account reflects entries for partners' drawing in equal amounts.

In July, 1967 the taxpayers opened a checking account with each individual signing the signature card as a partner in McManus, Chick and Gutleben, Et Al.[11/] The signature card authorizes the bank to conduct business with any of these individuals. Petitioner, on two separate occasions in correspondence with the respondent protesting changes to

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11/ The record does not disclose any apparent reason for the difference in the name of the entity from that appearing on the partnership returns.

his individual income tax return, stated that he was a member of a partnership known as McManus, Gutleben, and Chick and that Tract 2347 was its asset.

Petitioners argue that the taxpayers never intended to enter into a partnership, that there is no existing written or oral partnership agreement, and that the partnership tax returns were filed merely as a matter of convenience. The support for their first contention rests mainly on the testimony of petitioner, the sole surviving member of the group. While we have no reason to doubt his statements, we believe the substantive evidence, as discussed above, provides us with a better standard with which to judge the relationship of the taxpayers.

It does appear that there is no existing written partnership agreement. However, we have found that the taxpayers have been engaged in this and other activities over a substantial period of time. We have also found that large amounts of money and a substantial degree of personal effort were needed to further this activity. We can only believe that over the years the taxpayers discussed their rights and obligations between themselves and came to some understandings.

Petitioners maintain that the partnership returns were filed only as a matter of convenience and that they do not truly reflect their actual relationship. However, we have found that on several occasions the taxpayers have held themselves out as partners to third parties, and have acted individually on behalf of the others. We have also found the taxpayers have conducted substantial activities with respect to Tract 2347.

Petitioners argue that our earlier decision in Mihran Demirjian, supra, is distinguishable since in that case the office building was held by the taxpayers as partners and in the instant case Tract 2347 was held by the taxpayers as their separate property. However, as noted in Demirjian there are several elements to be measured in this determination and we believe that upon consideration of the evidence in this case the entity created by the taxpayers can be properly classified as a partnership.

Having made the above determination we can now move on to consider the oft-litigated issue of whether the real property owned by the partnership was held "primarily for sale to customers in the ordinary course of [its] trade or business" within the meaning of section 1221(1) or section 1231(b)(1)[12/] with the result that gain upon its sale is to be treated as ordinary income rather than capital gain. This issue is purely factual, its resolution depending on the unique combination of its particular facts.

To help place this issue in perspective several factors have been established as

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12/ Sec. 1231(b). Definition of Property Use in the Trade or Business. -- For purposes of this section --

(1) General Rule. -- The term "property used in the trade or business" means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 167, held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not --

particularly relevant. Those considered most often are:

> (1) the nature and purpose of the acquisition of the property and the duration of the ownership; (2) the extent and nature of the taxpayer's efforts to sell the property; (3) the number, extent, continuity and substantiality of the sales; (4) the extent of subdividing, developing, and advertising to increase sales; (5) the use of a business office for the sale of the property; (6) the character and degree of supervision or control exercised by the taxpayer over any representative selling the property; and (7) the time and effort the taxpayer habitually devoted to the sales.

United States v. Winthrop, 417 F.2d 905, 910 (5th Cir. 1969). However these factors have no independent significance and only form part of the entire situation presented. United States v. Winthrop, supra at 910.

Section 1221 defines the term "capital asset" as being property (with five statutory exceptions) held by the taxpayer. The

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12/ (Continued)

(A) Property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year.

(B) Property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business *** .

first statutory exception, as found in section 1221(1), excludes from the definition of propery:13/

> (1) stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business *** .

The purpose of this exception, as stated by the Supreme Court's opinion in Malat v. Riddell, 383 U.S. 569, 572 (1966), is to differentiate between gain derived from the everyday operations of a business and gain derived from assets that have appreciated in value over a substantial period of time. The Court went on to hold that, as used in section 1221(1), "primarily" means "of first importance" or "principally," Malat, supra at 572. This statutory exception had previously been clarified in Dunlap v. Oldham Lumber Co., 178 F.2d 781, 785 (5th Cir. 1950) when the Court noted that the property must not only have been "held primarily for sale," but also for sale in the "ordinary course of business." See also Winthrop, supra at 911 and William B. Howell, 57 T.C. 546, 555 (1972).

Petitioners argue that the property was not acquired primarily for sale citing other reasons for the acquisition of the

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13/ Similar language is used in sec. 1231 (b)(1), see footnote 12, supra.

property. Petitioner testified that the property was acquired for use in leasing and rentals, to generate additional work for the construction companies controlled by the taxpayers, and for investment purposes. However, we do not believe that the evidence in the record supports a finding that the acquisition was made primarily for either of the first two reasons.

When the property was acquired the taxpayers requested SRI to make a preliminary study of the market for office space at the property's location. Their report, which was generally pessimistic, only recommended the construction of a relatively small office building. The taxpayers then were aware at the outset that the rental or leasing prospects were not encouraging.

Petitioner did testify to several serious but ill-fated negotiations, which included the development of drawings, with prospective tenants. We can only believe that the depressed rental market, as found by SRI, contributed to these breakdowns. The taxpayers did manage to secure several leases but they do not appear to be the type that they had originally intended.

The petitioners also argue that they expected the acquisition of the property to generate additional construction work for the companies that they controlled. However these expectations should also have been affected by the findings reported by SRI. We do not believe that this was the motivating reason for the acquisition. In fact, the taxpayers were only involved in the construction of two buildings on the property, with most of the ultimate purchasers assuming the responsibility for their own projects.

It seems clear from the record that the partnership acquired a prime tract of property in the industrial section of Oakland. We believe that this property was acquired and managed primarily for the purpose of eventual resale, hopefully at a profit. This leaves for determination whether the property was held for sale in the ordinary course of the partnership's business.

We note at the outset that the partnership has engaged in this activity for a long period of time. In 1954, it acquired property in Oakland, subdivided and improved it, and sold the individual plots by approximately 1960. Shortly thereafter the property in issue was acquired. We view the second acquisition as a replenishment of the partnership's supply of land.

With the acquisition of the property the partnership developed plans to subdivide it. The necessary documents were submitted and approved and the property was subdivided and improvments (including road construction and installation of sewerage, water, gas, and electrical facilities) were made.

We are aware that property does not lose its capital asset status merely because the taxpayer has improved his property through his own efforts. Such activity does not always produce profit derived from the everyday operation of a business. United States v. Winthrop, supra at 908-909. However, the record indicates that the improvements greatly increased the value of the property and this, coupled with the partnership's prior history, provides us with tangible evidence of the partnership's intentions.

The parties are in direct conflict with respect to the effect of the sales activity regarding the property. Respondent points to the magazine advertisements, the real estate brokerage listing, and the activity of the real estate brokers in the area. Most of this activity does not appear to have been generated by the taxpayers although the evidence in this regard is sparse. If the taxpayers did not encourage this activity they certainly could have put the clamps on it. It seems clear to us that the taxpayers, the partners, held themselves out to the community as purveyors of raw land.

Petitioners point to the small number of sales, the particular reasons for some of them, and the length of time they held the property. We do note that holding an asset for several years indicates an intention to hold for investment, rather than for sale. Austin v. Commissioner, 263 F.2d 460 (9th Cir. 1959). However, we believe that factors have been established that negate these elements.

This property was acquired in 1961 at a time when the area was still developing. The neighboring sports stadium complex and the rapid transit system were still in their early development stages. We believe the taxpayers were waiting for this area to develop fully before they would sell.

The problems associated with the condemnation sale, which occurred in 1968, also contributed to the holding period of the property and deterred prospective purchasers who would be unsure of the desirability of this location. Gutleben's letter to the state in 1966 complains of delays and their effect on the partnership's use of the

property.

Petitioner points out that, of the five sales during the years in issue, two were attributable to condemnation or threatened condemnation action and two were connected with prior sales. As will be discussed later, we believe the former sales represent transactions made in the normal course of the petitioner's business.

Finally we note that the partnership return filed in 1962 reported the real estate profits for sales as ordinary income, thereby conceding the nature of their business for that year at least. We are also impressed with the large profits the partnership reaped through the years from its real estate activity.

Upon review of the evidence we have found factors to which both sides can point to support their position. Our determination is based upon an evaluation of those factors that have occurred over a period of years. See Starke v. Commissioner, 312 F.2d 608 (9th Cir. 1963), reversing 35 T.C. 18 (1960). After careful consideration of the total factual pattern in this rather closely contested issue, we find as an ultimate fact that the partnership was engaged in the real estate business. Consequently, we hold that the property was primarily held for sale to customers in the ordinary course of its trade or business. In view of this finding, the gain produced by the disputed sales is held to have resulted in the realization of ordinary income.

Petitioners argue even if we were to make the above finding, that the gain produced by the sales to the State of California

in 1968 and 1970 under an actual condemnation action and the threat of condemnation, respectively, are entitled to be treated differently and should receive long-term capital gain treatment. They argue that, once the prospect of condemnation materialized, the plots involved were no longer held for sale to customers in the ordinary course of the partnership's business.

In support of their position they have cited several recent decisions. However, upon careful review, we find them to be distinguishable from the situation at hand. In Casalina Corp., 60 T.C. 694, 703 (1973), affd. per curiam 511 F.2d 1162 (4th Cir. 1975) and Maurice F. Fabiani, T.C. Memo. 1973-203 this Court found that the property involved was held for investment purposes making a discussion of the condemnation factor immaterial.

In Ridgewood Land Co., Inc., T.C. Memo. 1972-16, Juleo, Inc., T.C. Memo. 1971-68 and TRI-S Corp., 48 T.C. 316 (1967), there is a finding that the respective taxpayers were in the business of developing real estate for residential or commercial purposes and that the condemnation action frustrated their original intentions. Since the original purpose for which the land was held had changed this Court held that they were entitled to report the gain realized on the condemnation sale as a long-term capital gain. This holding was affirmed in Ridgewood Land Co., Inc. v. Commissioner, 477 F.2d 135 (5th Cir. 1973) affd. per curiam, and Commissioner v. TRI-S Corp., 400 F.2d 862 (10th Cir. 1968); and was reversed in Juleo, Inc. v. Commissioner, 483 F.2d 47, 49 (3d Cir. 1973), cert. denied 414 U.S. 1103 (1973) where the court held that "a condemnation notice does not change land held primarily for sale to customers in

the ordinary course of business into a capital asset."

In the case at hand we do not believe that the condemnation factor changed the partnership's intention in the manner found by this Court previously. From the evidence in the record we believe that the partnership was in the business ab initio of purchasing raw land, improving it, and holding it for sale in that condition to prospective customers. Various governmental authorities could use the property in that condition and as such they represented potential customers for the partnership's property.

The record indicates that the partnership recognized the various governmental authorities as potential customers. Besides the two transactions in issue, there was a sale to the City of Oakland in 1962, and there were negotiations with respect to the construction of a post office. Furthermore, it appears that the amount paid by the state represented the amount that would have been paid by any other potential customers.

In our view, the condemnation element did not bring any unexpected customers to the partnership's door, but rather served as the means by which the sale was conducted. We see no reason then why the gain produced by the sales to its governmental customers should be treated any differently than the gain realized by sales to its other customers. Petitioners' argument must be denied.

Finally, having found that the entity created by the taxpayers constituted a partnership, we must now determine whether the election made individually by petitioners purportedly under section 1033, following

their individual reinvestment of the proceeds, is sufficient to defer the gain realized on the condemnation sale.

Petitioners argue that a partnership is not a taxable entity and that Thomas McManus, in his separate capacity, is liable for income taxes. Since the tax liability is determined at his level, they contend it follows that he individually, and therefore also his spouse, is entitled to the benefits of section 1033.

This question and these arguments were presented to this Court and decided adversely to the taxpayer in Mihran Demirjian, supra at 1698-1701. We see no need to repeat here what we said in that case. Suffice it to say that we find our previous opinion controlling and we intend to apply it to the issue at hand.[14/] Respondent's determination with respect to this issue must be upheld.

Decisions will be entered

under Rule 155.

14/ Having determined the petitioners' individual election is insufficient to defer the gain realized, it is not necessary to discuss respondent's other objection as stated in his deficiency notice.

APPENDIX B

UNITED STATES COURT OF APPEALS,

NINTH CIRCUIT

THOMAS K. McMANUS and MARGARET F. McMANUS,
Petitioners-Appellants v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee.

ESTATE OF JOHN C. GUTLEBEN, Deceased,
UNITED CALIFORNIA BANK, Executor, and
VERA B. GUTLEBEN, Petitioners-Appellants,
v. COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee.

ESTATE OF ELEANOR and NELSON CHICK, Deceased,
NELSE CHICK SILER, Executrix, Petitioner-
Appellant v. COMMISSIONER OF INTERNAL
REVENUE, Respondent-Appellee.

Nos. 76-1527
76-1528
76-1531
76-1760
76-1761
76-1532

(Opinion by Sterrett, J.) affirmed
Years 1968-1971.

Decision for Government

Petition to Review a Decision of The Tax Court of the United States.

Before CARTER, Circuit Judge, KUNZIG, Judge,* and TANG, Circuit Judge.

TANG, Circuit Judge:

The taxpayers[1/] appeal from a decision of the tax court, published at 65 T.C. 197 (1975), upholding the Commissioner's assessment of additional income taxes. We affirm.

Most of the facts were stipulated. The taxpayers were long-time associates in two construction companies. In 1954, they purchased a tract of land in Oakland, California. The tract was subdivided, and streets and utilities were installed. The subdivided parcels were then sold, with the last sale occurring in 1960.

In 1961, the taxpayers acquired a second tract. Tract 2347, which is the subject of this appeal. Tract 2347 is prime

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*HONORABLE ROBERT L. KUNZIG, Judge of the United States Court of Claims, sitting by designation.

1/ As used in this opinion, the term "taxpayers" refers to Thomas McManus, John Gutleben, and Nelson Chick. All three men filed joint returns with their wives for the years in question, but their wives had no other connection with the transactions involved and though parties to this action they are not separately referred to. Gutleben died in 1972 and his estate was substituted for him in this suit. Chick died in 1975 and a similar substitution was made.

industrial real estate, and is located directly across the freeway from the taxpayers' earlier tract. Title was taken as tenants in common. The property, about 36½ acres, was purchased for $926,000.00.

Shortly after the purchase, the taxpayers applied to the city planning commission for permission to subdivide the property. A plat was filed in May, 1962, showing 14 separate plots and a street.

Between March and September, 1962, the taxpayers spent about $240,000.00 installing roads, sewer lines, water, gas and electrical facilities. The taxpayers also commissioned a study by the Stanford Research Institute on the feasibility of building an office building on the site. The report was generally unfavorable.

At various times between 1963 and 1973 portions of Tract 2347 were leased. The leases were for pipe storage, amusement rides, billboard advertising and car parking. All these leases were for short periods and the tax court found the total rental income over the period was nominal.

Between 1961 and 1973, various parcels of Tract 2347 were sold, and a parcel was condemned by the State of California. The parties disagree as to how many sales occurred during the period. The taxpayers claimed that there were only eight voluntary sales, while the Commissioner asserted that there were at least 15 sales.[2/] The

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2/ Part of this discrepancy may be due to a difference of opinion on what constitutes a "voluntary" sale. Apart from the parcel

property was listed in the Western Real Estate News, the California Site Selection Handbook, and publications of the California Chamber of Commerce. Each of these publications received wide circulation within the real estate industry. The taxpayers did not authorize the inclusion of Tract 2347 in these publications, nor did they take any steps to remove the listings though they were aware of them. The listings were made without charge. At one time, a broker was given an exclusive listing for one parcel. The tax court found that it was generally known among brokers that Tract 2347 was available for sale or lease. The taxpayers' connection with Tract 2347 ended in 1973 when the remaining portions of the property were sold to the Continental Development Company. At the time of this sale, Gutleben had died, and Chick was in poor health.

From 1961 to 1970, the financial transactions regarding the property were recorded by the taxpayers in a system of books that listed the property as an asset of McManus, Gutleben and Chick. Some of

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2/ (Continued)

taken by the State of California, another parcel was acquired by the California Department of Motor Vehicles. The Department does have condemnation power though it was not used in this instance because the parties were able to agree on a price. After the California condemnation, the taxpayers agreed to exchange a parcel previously sold to Shell Oil Co. for another parcel. The original Shell parcel lacked highway access after the condemnation.

the entries in this account are labelled "Drawing 3 Partners". Such draws were made in equal amounts to the individual taxpayers. In 1967, the taxpayers opened a bank account at the United California Bank in San Leandro, California; the signature card indicated all three were co-partners and the card was signed in their capacity as partners. From 1961 to 1970 partnership tax returns were filed in the name of McManus, Gutleben and Chick, which included the Tract 2347 transactions. After 1970, on the advice of counsel, the filing of partnership returns was discontinued. During the course of the audit preceding this suit, McManus wrote two letters to the Internal Revenue Service which stated that Tract 2347 was owned by the partnership of McManus, Gutleben and Chick, and that he was a member of the partnership.

In 1968, after the California condemnation, McManus purchased property in Fremont, California which he believed constituted replacement property under 26 U.S.C. §1033. McManus did not notify the Commissioner that he had purchased replacement property until after April 1, 1970. No election under 26 U.S. C. §703 was ever filed on behalf of the partnership.

In their individual tax returns, the taxpayers claimed the gain realized on the California condemnation as capital gains. On previous returns, gains from the sale of parcels of Tract 2347 had been reported as ordinary income. During the audit the taxpayers signed Form 872-A which provided for an extension of the statute of limitations for tax year 1968 until 90 days after either the Commissioner or the taxpayer gave written notice to the other revoking

the extension. The Commissioner, on March 23, 1973, assessed deficiencies against the taxpayers on the basis that gain realized from Tract 2347 was ordinary income and not capital gains as reported.[3/] The matter was heard by the tax court, which found for the Commissioner on all counts. The taxpayers now bring this appeal.

The taxpayers raise four issues. They claim that Form 872-A was ineffective, and therefore the assessments for 1968 were beyond the statute of limitations. They claim that the tax court erred in finding that Tract 2347 was not a capital asset and in finding that Tract 2347 was owned by a partnership. Finally, McManus claims that the tax court erred in holding that he could not avail himself of the benefits of 26 U.S.C. §1033. Each of these matters will be discussed in turn.

A. The Statute of Limitations

[1] The statute of limitations, 26 U.S.C. §6501, provides for a three year assessment period for income taxes, §6501(a). However, §6501(c)(4) also provides.

3/ The amounts assessed were as follows:

	McManus	Gutleben	Chick
1968	43,235.00	21,897.00	25,538.00
1969	1,120.00	1,577.00	1,667.00
1970	21,861.00	22,510.00	22,622.00
1971	1,113.00	0	0
Total	67,332.00	45,984.00	49,827.00

> Where, before the expiration at the time prescribed in this section for the assessment of any tax imposed by this title, except for the estate tax provided in chapter 11, both the Secretary or his delegate and the taxpayer have consented in writing to its assessment after such time, the tax may be assessed at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon.

Absent an extension the assessment period for the tax year 1968 would have expired on April 15, 1972. The Commissioner issued the deficiency notices March 23, 1973.

The taxpayers argue that the form which they signed (Form 872-A)[4/] is ineffective under the language quoted above because it does not set a definite time when

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4/ Form 872-A, in pertinent part, reads as follows:

That the amount(s) of any Federal income tax due under any return(s) made by or on behalf of the above-named taxpayer(s) for the tax year(s) ended...under existing or prior revenue acts, may be assessed at any time on or before the 90th day after (1) mailing by the Internal Revenue Service of written notification to the taxpayer(s) of termination of Appellate Division consideration, or (2) receipt by the Regional Appellate Division branch office considering

the limitations period would end. In the taxpayers' view, Form 872-A extends the limitations period forever contrary to the intent of §6501(c)(4). We are not persuaded.

This form does not, as the taxpayers contend, extend the limitations period forever. The tax court held that the waiver would be accepted and operative for a reasonable time only. The taxpayers do not contend that the assessment here, filed 11 months after the three year period, were unreasonably delayed, nor could they prevail on such a contention.

Nor does §6501(c)(4) demand the reading the taxpayers give it. The statute

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4/ (Continued)

the case of written notification from the taxpayer(s) of election to terminate this agreement, except that if in either event a statutory notice of deficiency in tax for any such year(s) is sent to the taxpayer(s), the running of the time for making any assessment shall be suspended for the period during which the making of an assessment is prohibited and for 60 days thereafter. If such statutory notice is sent to the taxpayer(s) and neither of the conditions enumerated (1) and (2) in the preceding sentence have occurred, the time for making such assessment will expire 60 days after the period during which the making of an assessment is prohibited. However, this agreement will not reduce the period of time otherwise provided by law for making such assessment.

requires an agreement between the taxpayer and the Commissioner; it does not require an agreement for a fixed period of time. If a fixed period is agreed to, it can be extended. The taxpayers could have cut the extension period to 90 days by sending a letter. They failed to do so. We fail to see any significant difference between not sending a letter here and granting a further extension. A similar agreement was upheld in United States v. Mortell, 248 F. Supp. 706 [16 AFTR 2d 6047] (N.D. Ill. 1965). We hold that the 1968 assessments were not beyond the limitations period.

B. Capital Asset

[2, 3] The question here is whether Tract 2347 was "property held...primarily for sale to customers in the ordinary course of...trade or business" within the meaning of 26 U.S.C. §1221(1). The taxpayers contend they bought the property and held it for investment and rental purposes. The Commissioner asserts the taxpayers were in the business of buying raw land, developing it, and selling it for profit, and that their activities with regard to Tract 2347 were part of this business.

In this circuit, a finding that a particular asset was or was not a capital asset is a finding of fact and must be upheld unless clearly erroneous. Rule 52(a), Fed.R. Civ.P.: Parkside, Inc. v. Commissioner, 571 F.2d 1092 [41 AFTR 2d 78-451] (9th Cir. 1977); Los Angeles Extension Co. v. United States, 315 F.2d 1 [11 AFTR 2d 1162] (9th Cir. 1963). The case law has

developed a series of factors to be evaluated in determining whether land is held for sale in the ordinary course of business. These factors are:

> The length of holding of the property, the nature of the acquisition of the property, the frequency and continuity of sales over an extended period of time, the nature and the extent of the taxpayer's business, the activity of the seller about the property, and the extent and substantiality of the transactions.

Parkside, supra at 1096 quoting Los Angeles Extension Co., 315 F.2d at 3.

Applying these factors to the facts here, we can not say that the tax court's finding was clearly erroneous. The taxpayers spent considerable time, money and effort in subdividing and improving the land; the sales were reasonably constant over time; there was active promotion of the site, which the taxpayers did not discourage; and the short-term leases which were granted were consistent with a desire to sell the property. Further, the taxpayers had been involved in a prior land development operation, thus, their activities with respect to Tract 2347 can reasonably be viewed as a continuation of their land development business. The taxpayers' contentions that the land was held primarily for leasing purposes is not necessarily supported by the record. The leases entered into were short-term at nominal rentals. The taxpayers' own study showed the site was not favorable for rental purposes. Parcels of land were sold. The

contention that the sales were part of a liquidation is arguable. The sale to Continental Development Co. in 1973 may have been a liquidation but that was after the tax years involved here. The tax court's finding that Tract 2347 was held for sale in the ordinary course of business is not clearly erroneous and must be affirmed.

The taxpayers make a further argument that even if the property was held for sale in the ordinary course of business, once the State of California began condemnation proceedings, their holding of the condemned parcel changed to one for investment because the taxpayers could no longer sell the property. The circuits are presently in disagreement as to the effects of condemnation in these circumstances. The Fifth Circuit agrees with the taxpayers' argument, Ridgewood Land Co. Inc. v. Commissioner of Internal Revenue, 477 F.2d 135 [31 AFTR 2d 73-970] (5th Cir. 1973). The Third Circuit views the condemnation as merely the method of effecting the sale of the property, the court noted that the price paid for the condemned land included the value of the improvements and was affected by the surrounding sales. Juleo, Inc. v. Commissioner of Internal Revenue, 483 F.2d 47 [32 AFTR 2d 73-5275] (3rd Cir. 1973) cert. denied. 414 U.S. 1103, 94 S.Ct. 737, 38 L.Ed.2d 559. We agree with the reasoning of the Third Circuit. The taxpayers had negotiated with various governmental agencies about the sale or lease of parts of Tract 2347. One parcel was purchased by the California Department of Motor Vehicles. Condemnation proceedings in this context meant only that the parties were unable to agree on the price, not that the character of the holding of

the land was changed. See Stockton Harbor Industrial Co. v. Commissioner of Internal Revenue, 216 F.2d 638, 656 [46 AFTR 1055] (9th Cir. 1954) cert. denied 349 U.S. 904, 75 S.Ct. 581, 99 L.Ed. 1241 (1955).

C. Partnership

The tax court found that the taxpayers had conducted their land business as a partnership. Whether this finding was correct matters only with respect to McManus' election under 26 U.S.C. §1033. This finding was not erroneous.

[4] Partnership for tax purposes is broader than common law partnership. See 26 U.S.C. §761(a); Regs. §1.761(a). Here the taxpayers kept their account books on a partnership basis, opened a partnership bank account, and most importantly filed partnership tax returns. That title to the land was taken as tenants in common is not determinative since that may be considered neutral evidence. A taxpayer is estopped from later denying the status he claimed on his tax returns. See In re Steen, 509 F.2d 1398, 1402 n. 4 [35 AFTR 2d 75-623] (9th Cir. 1975); Demirjian v. Commissioner of Internal Revenue, 457 F.2d 1 [29 AFTR 2d 72-741] (3rd Cir. 1972); Maletis v. United States, 200 F.2d 97 [42 AFTR 923] (9th Cir. 1952) cert. denied 345 U.S. 924, 73 S.Ct. 782, 97 L.Ed. 1365 (1953).

D. McManus' Election under 26 U.S.C. §1033

[5] Under the provisions of 26 U.S.C. §1033(a)(3) the gain realized when property

is involuntarily converted will not be recognized if the proceeds are reinvested in similar or related property. Condemnation is a type of involuntary conversion. But §1033 is effective only if a proper election to defer recognition is made.

In this case only McManus, in his individual capacity, purchased replacement property. The tax court held that the election had to be made by the partnership under the terms of 26 U.S.C. §703(b), and McManus' election was therefore invalid. Demirjian v. Commissioner of Internal Revenue, 457 F.2d 1 [29 AFTR 2d 72-741] (3rd Cir. 1972) is exactly on point and supports the tax court.

McManus argues that since a partnership is not a taxable entity, each partner can make his own elections. While it is true that a partnership is not liable for tax, the rest of the argument fails. A partnership is required to file returns, 26 U.S.C. §6031, and the partners are required to conform their individual returns to the partnership returns. If each partner could determine his share of the partnership income separately, confusion would result, confusion which Congress meant to avoid by enacting 26 U.S.C. §703(b). The tax court is correct on this point.

Affirmed.